



IRS Issues Clarifying Guidance on the PATH Act Changes to Section 179 and Bonus Depreciation

Summary

The Protecting Americans from Tax Hikes Act of 2015 ("PATH Act" or "The Act") included amendments and changes to §§179, 168(k), and 168(j). The changes made in The Act are effective for property placed in service in taxable years beginning in 2016. A major impact of The Act is the creation of a new category of qualified property, called qualified improvement property, eligible for the additional first-year depreciation deduction (bonus depreciation) under §168(k). The IRS recently issued Revenue Procedure 2017-33, which provides guidance and examples to clarify the application of the qualified improvement property classification, as well as guidance on other changes made to §§179, 168(k), and 168(j) by The Act.

Background

On December 18, 2015, Congress enacted the PATH Act (P.L. 114-113).

Section 179(a) allows a taxpayer to elect to treat the cost (or a portion of the cost) of any §179 property as an expense for the taxable year in which the taxpayer places the property in service. The Act amended §179 by:

1. making permanent the treatment of qualified real property as §179 property under § 179(f),
2. making permanent the permission granted under §179(c)(2) to revoke without consent of the Commissioner of Internal Revenue any election made under §179 and any specification contained in that election, and
3. allowing certain air conditioning or heating units to be eligible as §179 property under §179(d)(1).

Prior to amendment by the PATH Act, §168(k)(1) allowed a 50-percent additional first year depreciation deduction for qualified property that was acquired by a taxpayer after 2007 and placed in service by the taxpayer before 2015 (before 2016 in the case of certain long production period property and certain noncommercial aircraft). The Act amended §168(k) by:

1. extending the bonus depreciation allowance to qualified property placed in service before January 1, 2020 (or before January 1, 2021, in the case of certain long production period property and certain noncommercial aircraft),
2. modifying the definition of qualified property under §168(k)(2),
3. extending and modifying the election under §168(k)(4) to increase the alternative minimum tax (AMT) credit limitation, in lieu of the additional first year depreciation deduction (Rev. Proc. 2017-33 does not include guidance on this section),
4. adding §168(k)(5), which allows a taxpayer to elect to deduct the additional first year depreciation for certain plants bearing fruits and nuts before such plants are placed in service,
5. adding §168(k)(6), which provides a phase down of the additional first year depreciation deduction percentage for future taxable years, and
6. adding §168(k)(7), which allows a taxpayer to elect not to deduct additional first year depreciation for any class of property.

Internal Revenue Code §168(j) – Property on Indian reservations, provides the applicable recovery periods



for qualified Indian reservation property and special rules pertaining to such property. The Act amended §168(j) by adding §168(j)(8), which allows a taxpayer to elect not to apply §168(j) for any class of property.

The IRS issued Rev. Proc. 2017-33 to provide guidance on the changes made by The Act in response to taxpayer questions regarding these changes. The revenue procedure does not reflect any proposed technical corrections to The Act. The following discussion briefly highlights certain key points discussed in Rev. Proc. 2017-33. Rev. Proc. 2017-33 is effective as of April 20, 2017.

Air Conditioning Units Qualifying as §179 Property

Rev. Proc. 2017-33 clarifies that, in addition to portable air conditioning or heating units meeting the requirements to be classified as §179 property, if a component of a central air conditioning or heating system meets the definition of qualified real property, as defined in §179(f)(2), and the component is placed in service by the taxpayer in a taxable year beginning after 2015, the component may qualify as §179 property if the taxpayer elects to apply §179(f).

As provided in §179(f)(2), qualified real property includes qualified leasehold improvement property, qualified restaurant property, and qualified retail improvement property.

Acquisition Date Requirement for Qualified Property

Qualified property described under §168(k)(2)(A) no longer has to meet the acquisition date requirements in §168(k)(2)(A)(iii) that were in effect prior to the enactment of The Act. Property acquired after December 31, 2007, and before January 1, 2020, that meets all other requirements of §168(k), is qualified property.

Note that The Act imposes a new acquisition date requirement for property described in §168(k)(2)(B) and (C) (i.e. long production period property and certain aircraft).

Placed-In-Service Date Requirement for Qualified Improvement Property

Qualified improvement property is defined in §168(k) as “any improvement to an interior portion of a building which is nonresidential real property if such improvement is placed in service after the date such building was placed in service.”

The term “first placed in service” means the first time the building is placed in service by any person.

Rev. Proc. 2017-33 provides several examples illustrating that improvements placed in service any time after the building is placed in service, even one day later, can qualify for bonus depreciation. This includes the initial build out of tenant spaces in a commercial rental building as discussed in example 4 of the revenue procedure.

Qualified Restaurant Property

Qualified property that is placed in service by the taxpayer after December 31, 2015, and that meets the definition of both qualified improvement property and qualified restaurant property, as defined in §168(e)(7), is eligible for the additional first-year depreciation deduction under §168(k), assuming all other requirements in §168(k) are met.

Rev. Proc. 2017-33 provides two examples illustrating when qualified restaurant property is, or is not, also qualified improvement property.

Phase Down of Additional First-Year Depreciation Percentage

Two tables in Rev. Proc. 2017-33 provide the additional first-year depreciation deduction percentages for qualified property placed in service by the taxpayer after 2015 and before 2020 (2021 for property described in §168(k)(2)(B) or (C)). The first table addresses property that is not described in §168(k)(2)(B) or (C) and the second table addresses property that is described in §168(k)(2)(B) or (C) (i.e. long production period property and certain aircraft).



Other Guidance Provided by Rev. Proc. 2017-33

In addition to the guidance addressed above, Rev. Proc. 2017-33 provides guidance for other areas of §§179, 168(k), and 168(j) affected by The Act, including making §179 elections by amended returns, rules for making the election under §168(k)(7) not to deduct the additional first-year depreciation deduction, special rules for certain plants bearing fruits and nuts and the §168(k)(5) election for a specified plant, and the §168(j)(8) election not to apply §168(j).

Insights

Taxpayers should be aware of all the requirements to take advantage of the qualified improvement property asset classification. Due to the fact that qualified improvement property is eligible for the additional first-year depreciation deduction, proper application of the qualified improvement property classification can provide an opportunity for substantial depreciation deductions in certain situations.